



UT Health

San Antonio

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Date: August 21, 2019

To: James Kazen, Executive Vice President, Facilities Planning & Operations

From: John Lazarine, Chief Audit Executive
Internal Audit & Consulting

Subject: Audit Report – Facilities Management – Change Orders

As part of our approved Audit Plan, we recently completed an audit of Facilities Management – Change Orders. Attached is the report detailing the results of this review. Management's Action Plans are included in the report.

We appreciate the cooperation and assistance we received from Facilities Management and Purchasing throughout the review.

Respectfully,

John Lazarine, CIA, CISA, CRISC
Chief Audit Executive
Internal Audit & Consulting Services

Distribution:

cc: Dr. William Henrich, President
Michael Black, Sr. EVP & COO
Andrea Marks, VP & CFO
Yeman Collier, VP & CIO
Jack Park, Chief Legal Officer
Daniel Costello, Associate Vice President, Facilities Management
Eric Walls, Senior Director, Supply Chain Management
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Pat Frost
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**Facilities Management – Change Orders
Audit Report (18-03)
August 21, 2019**

Summary of Audit Results

Background Information

The Office of Facilities Management (Facilities) is responsible for the planning, construction, operation and maintenance of general fund supported academic and administrative buildings, campus grounds, and all utility, energy and building management systems. Facilities staff review and approve project change orders to extend project timelines and amend contract costs due to changes in the scope of work. As of June 4, 2019, the budget for active capital projects in AiM¹ totaled \$129.9 million. This includes projects managed by Facilities and those that were initially managed by the UT System Office of Facilities Planning & Construction (OFPC)², and includes costs reported for work performed by external contractors and internal Facilities trades.

Objective and Scope

The objective of this audit was to assess the adequacy and effectiveness of internal controls over the change order management process. The scope of this audit included a sample of change orders processed for projects during the period of September 1, 2017 through March 31, 2019. Specifically, we focused on projects managed by Facilities for work performed by external contractors, as opposed to work performed by Facilities trades.

We conducted our audit in accordance with the Institute of Internal Auditors' *International Standards for the Professional Practice of Internal Auditing*.

Summary of Results

Overall, the adequacy of internal controls over the change order management process is sufficient. However, opportunities to further strengthen these processes and controls were identified, such as including additional detail in the justification for a change order and enhancing monitoring procedures regarding surety bonds and insurance policies. Additionally, Institutional procurement policies should be clarified to ensure the appropriate level of approval for amending construction contracts is obtained.

Observations, recommendations and management's action plans are detailed in the attached table of Issues and Recommendations. We appreciate the courtesy and cooperation we received from staff within Facilities and Purchasing throughout this audit.

Summary of Priority Findings

Based on the results of this audit, there were no findings considered to be Priority to the Institution. The UT System Internal Audit finding Classification System includes Priority, High, Medium, or Low-level findings. A Priority Finding is defined as an issue identified by an internal audit that, if not addressed timely, could directly impact achievement of a strategic or important operational objective of a UT institution or the UT System as a whole. Non-Priority Findings are ranked as High, Medium, or Low, with the level of significance based on an assessment of applicable risk factors and probability of a negative outcome occurring if the risk is not adequately mitigated.

¹ AiM is the project management system used by Facilities.

² As part of a strategic alignment by UT System, as of June 3, 2019, projects managed by the OFPC will be managed by UT Health San Antonio.

Distribution

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Mr. Yeman Collier, Vice President and Chief Information Officer
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Approved
for Release



John Lazarine, Chief Audit Executive, Internal Audit & Consulting Services

Issues and Recommendations

Facilities Management – Change Orders

	Observation/Condition	Business Implication	Recommendation	Management Action Plan	Due Date	Responsible Party
Change Order Documentation						
1	<p>Justification for Change Order</p> <p>Change order documentation did not consistently contain sufficient justification for why a change in the original scope of work was necessary. Specifically, 12 of 17 change orders reviewed, totaling \$196,386, often used the term “Unforeseen condition” to explain why a change order was needed.</p> <p><i>During the course of this review, Facilities updated internal policies to include additional guidance on use of specific project descriptions when making formal changes to the scope of work. For example, “unforeseen condition” may be used in a case where a special skill or service is required (i.e. asbestos removal) that was not known when the project was initiated, but not as a general reason for a change.</i></p> <p>Risk Rating: Medium</p>	<p>Insufficient detail for a change order could result in duplicate or additional work being conducted, which may inadvertently increase the cost of a project.</p>	<p>Use the new guidance to document any justifications for a change in the original scope of work for a given project.</p>	<p>Management has updated internal procedures to include additional guidance on the use of project descriptions when making formal changes to the scope of work and by adding additional supporting documentation.</p>	<p>Closed</p>	<p>N/A</p>

	Observation/Condition	Business Implication	Recommendation	Management Action Plan	Due Date	Responsible Party
Surety Bond & Insurance Validation/Monitoring						
2	<p>Validation of Surety Bonds and Insurance Policies</p> <p>Surety bonds are not adequately reviewed and monitored to ensure authenticity and appropriate value and coverage.</p> <p>Currently, Purchasing receives a copy of all surety and insurance documentation at the onset of a project. The bonds and insurance policy copies are included in the project file, but not validated. In addition, when project values are increased due to change orders, surety bonds are not verified to ensure the increase in value was obtained.</p> <p>Audit noted two instances where a contractor was paid to increase a bond value and it either was not done (\$374 loss) or was done several months later by the contractor. In both instances Facilities and Purchasing staff were unaware of this issue until Audit brought this matter to their attention.</p> <p>Risk Rating: Medium</p>	<p>Insufficient validation controls of surety and insurance coverage increases the Institution's risk of financial loss should the contractor not perform in accordance with the contract.</p>	<ol style="list-style-type: none"> 1. Validate surety bonds and insurance policies at the onset of a project and intermittently thereafter, as necessary, to ensure the Institution is adequately protected from financial harm. 2. In addition, staff should request a refund or credit of \$374 from the contractor for the bond that was not increased as required by the contract. 	<ol style="list-style-type: none"> 1. Management has updated procedures to implement a bonding and insurance review and monitoring process to ensure insurance certificates are valid and meet coverage requirements, and that bonds are valid and valued commensurate with the project values. 2. Management will pursue a credit or refund from the contractor. 	<p>10/1/19</p> <p>10/1/19</p>	<p>Sr. Director Supply Chain Management</p> <p>Director of Financial Operations for Facilities Management</p>

	Observation/Condition	Business Implication	Recommendation	Management Action Plan	Due Date	Responsible Party
Institutional Procurement Policy – Amending Contract Values						
3	<p>Procurement Policy – Amending Contract Values through Purchase Orders due to change orders.</p> <p>Institutional procurement policies have not been revised to ensure the appropriate level of approval for amending an original contract value. Currently, there are no Institutional policies regarding amending contracts through the change order process, which would result in the overall value of the contract being increased.</p> <p>The Institution's formal Delegation of Authority document states that a senior buyer may execute a purchase order for up to \$1 million, but does not specify whether the purchase order is within the original value or will increase the overall value of the contract.</p> <p>The Institution's formal Delegation of Authority document does not cover contract amendments and gives signature authority to execute a contract to only four³ individuals Institutional-wide to execute a contract up to \$10 million. In addition to the four executive signers, a Contract Administration Manager may also execute a contract, but only up to a maximum of \$15,000.</p> <p>Risk Rating: Medium</p>	Inappropriate signature authority increases the Institution's risk of financial loss.	Update current Institutional Policies to reflect appropriate approval thresholds for amending contracts and authorizing buyers to execute purchase orders.	<p>Management has updated Internal Purchasing Procedures to document additional controls in place, which includes Senior Director or Assistant Director review and approval of any purchase order, contract, or PO increase over \$250,000</p> <p>In addition, management plans to update Institutional policies to address contracts with links to Internal Purchasing procedures where applicable. All updates to Procurement's Internal policies have been completed and communicated to affected staff.</p>	Closed	Sr. Director Supply Chain Management

³ The four individuals include the Senior Director of Supply Chain Management, Chief Financial Officer, Chief Operating Officer, and Assistant Vice President for Business Affairs.